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China's new road to prosperity?

China has achieved unprecedented growth and poverty reduction — at the cost of rising inequality. Now, the CCP looks to rebalance 'growth and sharing'

China has seen unprecedented economic growth since the introduction of the open-door and reform policies in 1978, catapulting China from dire poverty to an upper-middle-income country. However, the past half century's rapid economic growth also poses serious distributional problems: widening income gaps, the disparity of regional and urban-rural developments, unequal access to public services, and unequal economic opportunities because of an unequal access to education.

Against this background, in 2020 the Communist Party of China (CPC) formally adopted 'common prosperity' as a goal, referring to a collection of economic and social policies balancing efficiency and fairness, growth and sharing.

Subsequently, the Chinese government has incorporated this objective in its Five-year Plan and its Long-term Goals for 2035, in order to address the 'side-effects' of rapid development. To put this policy development into perspective, one needs to look at the evolution of related policies in different development stages in China.

China's reform path

Prior to the reforms of 1978, China was a highly centralised planned economy. The government dominated almost all aspects of resource allocation. Since the founding of the People's Republic in 1949, the government deliberately kept wages low and relatively equal to facilitate capital accumulation. Between 1952 and 1986, China's overall inequality was among the lowest in the world.

The government saw low wages as an efficient path to industrialisation. However, the implementation of such policies seriously impaired incentives and greatly eroded economic efficiency. As a result, per capita income was only USD 156 in 1978, ranking one of the lowest in the

world. The rural population living in poverty reached 770 million in 1978 and the poverty rate was as high as 97.5 per cent.

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With the mostly lacklustre performance of the planned economy and the tremendous fiscal difficulties faced by the central government, China moved decisively to economic reform and liberalisation in 1978. Government policies shifted to 'efficiency first' by allowing market forces to dominate resource allocation. The transition to a market economy was mostly completed by the end of last century, coupled with the accession to the WTO that integrated the Chinese economy globally.

Market liberalisation aligned incentives and fostered rapid growth. No explicit income policy was pursued during this period. As a result, the gap between urban and rural incomes widened from USD 155 in 1978 to USD 3,375 in 2015, reflecting a serious distributional problem.

China's elimination of poverty

In the ongoing 'New Era,' China has again adopted explicit policies tackling distributional problems. Two phases can broadly be distinguished: in the first, policies were aimed at eliminating absolute poverty, and in the second, policies are now designed to achieve 'common prosperity'.

After Xi Jinping took over as General Secretary of the Communist Party of China (CPC), he proposed the idea of 'precise (targeted) poverty alleviation' during his visit to west Hunan in November 2013. Poverty alleviation then became the consensus of the whole CPC and governments at all levels, culminating in a series of policy initiatives devoting substantial resources to improve rural infrastructure and to incubate various forms of cooperatives in retaining rural local employment in a sustainable way. By means of targeted support – like cadres stationed in villages – these policy efforts produced remarkable results over seven years. By the end of 2020, all 832 of the poorest counties have been lifted out of poverty and, by Chinese standards, almost all absolute poverty was eliminated.

By eliminating absolute poverty, China has built a solid foundation for the second phase of policy-making: achieving 'common prosperity' to narrow distributional disparity further. Although it is not absolutely clear what 'common prosperity' actually encompasses, many of the currently

available policy documents indicate that it targets ex-ante equality.

Common prosperity as a political move

The CPC emphasised that 'the way to govern the country starts with enriching the people'. Accordingly, its 18th National Congress in 2015 put 'the gradual realisation of common prosperity for all people' in a more prominent position, and made it clear that common prosperity should be the fundamental principle and essential requirement of socialism with Chinese characteristics.

This objective was reinforced in the 19th National Congress of the CPC in 2017, setting out the goal of achieving 'common prosperity for all people by 2050,' with an interim goal of 'achieving more substantive progress in the common prosperity for all people by 2035.' This was reiterated by Xi Jinping in his CPC 100 Anniversary speech in 2021, emphasising that 'achieving common prosperity is not only an economic issue, but also a major political issue related to the party's governing foundation.' All these reflect the CPC's tremendous political drive to rejuvenate China.

The intention of policies associated with 'common prosperity' indicates the government's concern regarding social fairness and reflects China's comprehensive reform measures.

It is certain that China has an important political motivation to push forward policies to promote 'common prosperity'. The widening income inequality, coupled with high housing prices, impedes younger generations climbing the social ladder and the vertical mobility of lower income groups. This engenders social instability: social events such as petitions and group rallies have increased markedly during this period, resulting in potential political instability.

Common prosperity as an economic move

Politics aside, there could also be an economic rationale for these policies. The recent trade friction between the US and China indicates their heightened geo-political conflict, resulting in China's shift to the so-called 'dual-circulating' economy, reducing its reliance on bilateral trade in the event of conflicts. As increased inequality reduces the average propensity for consumption, it could lead to weak domestic demand and lower economic growth.

The intention of policies associated with ‘common prosperity’ indicates the government’s concern regarding social fairness and reflects China's comprehensive reform measures. Its core idea is the continuation of the principle of ‘let[ting] the market play a decisive role in resources allocation, complemented by government interventions if necessary.’

Policies of ensuring ex-ante equal opportunities include: significant fiscal transfers to compulsory education in less developed regions, restricting extra curriculum teaching activities outside schools, subsidising skill-related higher education courses and research and development activities in small and medium sized firms, and more provisions for on-job training. Ex-post interventions to make markets more effective are mainly reflected in competition policies to restrict monopoly powers of various internet platforms such as DiDi, WeChat, Meituan, and Alibaba.

In short, ‘common prosperity’ is essentially aimed at balancing efficiency and fairness, growth and sharing, so that the benefits of economic development can be more evenly distributed in the whole society. This collection of economic and social policies facilitates the creation of an all-inclusive growth model which provides ex-ante equal opportunities and minimises ex-post market distortions. It is a far-reaching and interesting social experiment, but it is too early to gauge the long-term effects of these policies.



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